HARVARD

LAW REVIEW.

VOL. XXIII. MAY, 1910. NO. 7.

EXECUTED ULTRA VIRES TRANSACTIONS.

THE sovereign charters a corporation, M. Its "powers" are defined. The natural persons incorporated assume, in the name of M, to do an act not within the scope of the "powers." What is the legal effect?

The law relating to *ultra vires* transactions presents three principal questions: (1) Shall an executed transaction be a foundation of rights and obligations? (2) Shall an executory transaction be a foundation of rights and obligations? (3) Shall an executed transaction be set aside? This article deals only with the first of these questions.

A corporation is a composite unit. The human mind readily conceives the notion of many persons forming a unit. Is this a fiction? The human mind conceives of a river as forming a unit, not simply as so many drops of water. It conceives of an army as forming a unit, not simply as so many soldiers. In this there seems to be no fiction, — no make-believe.

The conception of many human beings as one is not necessarily the conception of many human beings as one human being. A human being is a unit, but there are many units which are not human beings. Suppose the conception were of many human beings as one human being. Would this be a fiction? It seems to me that it clearly would. Suppose the conception were of many human beings as a unit, and that this unit had a mind and will of its own, similar to the mind and will of a human being. Would this be a fiction?

It may be said that there is no more difficulty in conceiving of many minds as forming a composite unit, in the way of minds, than

there is in conceiving of many bodies as forming a composite unit, in the way of bodies. It is a problem which goes beyond the law into philosophy, and beyond philosophy into religion. Many persons conceive of God as the sum of all consciousness, — that is, as a composite unit made up of all existing consciousnesses.

If to conceive that the unit has a mind and will of its own similar to the mind and will of a human being is not a fiction, then the reasoning of this article is, *a fortiori*, sound. I will therefore assume that it is a fiction, — a make-believe.

It is a popular make-believe, rather than a legal make-believe. It is to be found in the earliest and rudest literatures. The judges did not originate it. In ascribing to a corporation a mind and will similar to the mind and will of a human being, and in giving it rights and duties similar to the rights and duties of a human being, the law simply adopts and uses a convenient popular fiction.

Many human beings may act as though they formed a unit with a mind and will of its own. This is corporate action.

Suppose the sovereign authorizes them so to act. Just what is the effect of this authority? It does not affect the fiction at all. It does not originate the fiction. It does not make the fiction either greater or less. *It is equivalent to a direction to the judges to act upon the fiction in the specified case.* But the judges might have acted upon the fiction without any such direction. And — if they think it proper — they may to-day act upon the fiction without any such direction.

The law in early times recognized that there could be corporate action without the authority of the sovereign, and gave legal validity to such corporate action.[1]

Corporate action unsanctioned by the sovereign is as real as corporate action sanctioned by the sovereign. Unauthorized corporate action is as real as authorized corporate action. The question becomes: Is it ever proper for the judges to act upon the fiction in the absence of a direction from the sovereign, — is it ever proper for the judges to give legal validity to unauthorized corporate action?

Lord Coke seems to have conceived that there *could* be no corporate action except by the consent of the sovereign. The charter worked legal magic. It called forth a legal spook. The spook could not pass beyond the bounds laid down in the charter. Unauthorized

[1] See 21 HARV. L. REV. 308, and notes 1 and 2 appended to the text.

corporate action was, to Coke, unthinkable, — it was a contradiction in terms.[1]

If this view is taken, then, whenever natural persons who have been incorporated assume, in the name of the corporation, to do an act *ultra vires* of the corporation, the courts *cannot* give effect to the act, as the act of the corporation.

In Central Transportation Co. *v.* Pullman's Car Co., 139 U. S. 24, the court, speaking by Mr. Justice Gray, said: "A contract of a corporation, which is *ultra vires* in the proper sense, that is to say, outside the object of its creation as defined in the law of its organization, and therefore beyond the powers conferred upon it by the legislature, is not voidable only, but wholly void, and of no legal effect. The objection to the contract is, not merely that the corporation ought not to have made it, but that it could not make it. The contract cannot be ratified by either party, because it could not have been authorized by either. No performance on either side can give the unlawful contract any validity, or be the foundation of any right of action upon it." In California Bank *v.* Kennedy, 167 U. S. 362, a certificate for shares of the stock of corporation M was issued in the name of corporation N, and dividends thereon were paid into the treasury of N. M became insolvent, and a creditor sought to enforce against N the liability attaching to shareholders in M. The court allowed N to defend, on the ground that the purchase of the shares by N was *ultra vires*. "It would be a contradiction in terms to assert that there was a total want of power by any act to assume the liability, and yet to say that by a particular act the liability resulted. The transaction being absolutely void, could not be confirmed or ratified."

It is submitted that this reasoning is erroneous.

Consciously, or unconsciously, all courts to-day do treat some unauthorized corporate action as corporate action. For example: Persons have sought to become incorporated, but have failed to perform a condition precedent to incorporation. They nevertheless assume to act as a corporation. All courts, under some circumstances, treat this unauthorized corporate action as corporate action, and give legal validity to it as such.[2]

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[1] See 21 HARV. L. REV. 306, 307.

[2] These circumstances are stated and discussed in two articles on Collateral Attack on Incorporation in 20 HARV. L. REV. 456, and 21 HARV. L. REV. 305.

If, when the associates are not authorized to act as a corporation for any purpose, the courts can treat unauthorized corporate action as corporate action, they *can* do the same when the associates are authorized to act as a corporation for some purposes, but not for the purpose in question.

Unauthorized corporate action is legally objectionable. The sovereign may always object, and obtain relief. Assume, however, that the sovereign does not object; are the courts bound to allow private individuals to raise the point? The development of the doctrine that collateral attack on the formation of a corporation may be denied shows that the courts have not felt themselves bound to do so.

If a court may properly deny collateral attack on the formation of a corporation, it may conceivably be proper for it to deny collateral attack on the powers of a corporation which has been duly formed.

There was a time when the courts held that a corporation could not be liable for any tort, because it was not authorized to commit torts.[1] To-day such a doctrine is treated as absurd. May it not be equally absurd to assert that a corporation cannot be liable on a contract, because it was not authorized to make the contract?

The reasoning, given above, by Mr. Justice Gray sounds decisive and conclusive. Can these sonorous passages be taken at their ear value? It becomes profitable to review the leading cases bearing on the topic which have been decided by the United States Supreme Court itself.

Head v. *Providence Insurance Co.*, 2 Cranch 127 (1804). A contract of insurance, not executed according to the provisions of the charter of the defendant, was held not to be a corporate act. Marshall, C. J., said (p. 166): "This body . . . is the mere creature of the act to which it owes its existence. . . . The act of incorporation is to them an enabling act; it gives them all the power they possess; it enables them to contract, and when it prescribes to them a mode of

[1] "Trespas ne git vs cominaltie s. per le nosme de corporation, mes vs les persons q. ceo fieront p. lour proper nosmes." 22 Ass. p. 67.

"Corporation ne poet estre batus in lour corporation mes in lour natural corps ne corporation ne poet bater aut ne faire treason ou felony in lour corporation." 21 Edw. IV, 72.

These authorities were followed by Coke and Blackstone. 10 Co. 32 *b*; 1 Bl. Comm. 476.

contracting, they must observe that mode, or the instrument no more creates a contract than if the body had never been incorporated." [1]

Pearce v. *Madison Co.*, 21 Howard, 441, 444 (1858). A corporation gave notes for the purchase of property which it was not authorized to purchase, and it was allowed to defend against the endorsee of the notes. "The only question is, Had the corporation the capacity to make the contract, in the fulfillment of which they were executed?"

National Bank v. *Matthews*, 98 U. S. 621 (1878). A executed a promissory note to B, and, to secure the payment thereof, a deed of trust of lands which was in effect a mortgage with a power of sale. A national bank loaned money to B, and assumed to take an assignment of the note and deed. Making a loan on the security of real estate was *ultra vires* of the bank. The court, nevertheless, declined to enjoin the trustee from selling the lands for the benefit of the bank, saying (pp. 628–629): "Where a corporation is incompetent by its charter to take a title to real estate, a conveyance to it is not void, but only voidable, and the sovereign alone can object. It is valid until assailed in a direct proceeding instituted for that purpose. . . . The impending danger of a judgment of ouster and dissolution was, we think, the check and none other contemplated by Congress. That has always been the punishment prescribed for a wanton violation of a charter, and it may be made to follow whenever the proper public authority shall see fit to invoke its application. A private person cannot, directly or indirectly, usurp this function of the government."

National Bank v. *Case*, 99 U. S. 628 (1878). A corporation, N, assumed to take stock in a national bank, M. The receiver of M sought to charge N as a shareholder. The court held that, under the circumstances, the transaction was not *ultra vires*. "But if [otherwise] the lender could not set up its own violation of law to escape the responsibility resulting from its illegal action."

Cowell v. *Springs Co.*, 100 U. S. 55, 60 (1879). Corporation M assumed to be the owner of Blackacre, and to lease it to A upon a condition. The condition was broken, and M brought ejectment against A. A defended on the ground that ownership of Blackacre was *ultra vires* of M. The court permitted M to recover, and said that whether the holding of Blackacre was necessary to enable M to

[1] See also Bank of Augusta *v.* Earle, 13 Pet. 519; Perrine *v.* Chespeake Co., 9 How. 172.

carry on its business was a matter "between the government of the state . . . and the corporation, and is no concern of the defendant."

Thomas v. *Railroad Co.*, 101 U. S. 71, 86 (1879). Corporation M assumed to make a lease of its property to A. This was *ultra vires* of M. The lease provided that, if M resumed possession, there should be a payment to A, to represent the value of the unexpired term. M resumed possession, and the court held that it need not pay A. "What is sought . . . is the enforcement of the unexecuted part of the agreement. . . . It is not the case of a contract fully executed. . . . We cannot see that the present case comes within the principle that requires that contracts which, though invalid for want of corporate power, have been fully executed shall remain as the foundation of rights acquired by the transaction." [1]

Christian Union v. *Yount*, 101 U. S. 352, 361 (1879). A assumed to deed Blackacre to corporation M (apparently without consideration). A died, and his heirs sought to recover the land. "Its acquisition of a larger quantity of real estate than the charter allowed, or its business required, or was consistent with the law of Illinois, was not a question which the appellees have any right to raise. If the title passed by valid conveyance from their ancestor, it is of no concern to them that the appellant has acquired or is holding more real estate than its charter authorizes."

Jones v. *Guaranty & Indemnity Co.*, 101 U. S. 622, 628 (1879). Corporation M assumed to give a mortage which the mortgagee sought to enforce. "If [the mortgage] be *ultra vires*, no one can take advantage of the defect of power involved " but the state. As to all other parties, it must be held valid, and may be enforced accordingly. . . . In [National Bank *v.* Matthews] this subject was fully examined."

National Bank v. *Whitney*, 103 U. S. 99 (1880). A national bank was permitted to exercise the rights of a mortgagee although its holding the mortgage was alleged to be *ultra vires*. "The question presented is not an open one in this court. It was determined in the case of National Bank *v.* Matthews. . . . Judicial decisions affecting the business interests of the country should not be disturbed except for the most cogent reasons." [2]

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[1] See also Oregon Railway Co. *v.* Oregonian Railway Co., 130 U. S. 1, 37.

[2] National Bank *v.* Matthews was also followed in Swope *v.* Leffingwell, 105 U. S. 3, and in Fortier *v.* New Orleans Bank, 112 U. S. 439, 451.

Jones v. *Habersham*, 107 U. S. 174 (1882). Corporation M was authorized to hold property "provided that the clear annual income . . . shall not exceed the sum of five thousand dollars." A assumed by his will to give M certain property, and the clear annual income of the property previously held by M and of that assumed to be given was in excess of five thousand dollars. To the attack of the heirs and next-of-kin of A the court said (p. 188): "Restrictions imposed by the charter of a corporation upon the amount of property that it may hold cannot be taken advantage of collaterally by private persons, but only in a direct proceeding by the state which created it."

National Bank v. *Stewart*, 107 U. S. 676 (1882). M, a national bank, assumed to make a loan which was *ultra vires*. It sold the security. The debtor was held not entitled to recover the proceeds from the bank. The court said that it was too late for any one except the government to dispute the validity of the transaction.

Reynolds v. *Crawfordsville Bank*, 112 U. S. 413 (1884). A corporation M assumed to own Blackacre, and sought to restrain waste by A, the former owner. A alleged that the ownership by M was *ultra vires*. As an additional ground for giving the desired relief, the court said: "Where a corporation is incompetent by its charter to take a title to real estate, a conveyance to it is not void, but only voidable; the sovereign alone can object. It is valid until assailed in a direct proceeding instituted for that purpose." [1]

Salt Lake City v. *Hollister*, 118 U. S. 256 (1885). The plaintiff alleged that a tax was illegally exacted from it for the distilling of spirits. The spirits were distilled by the officers of the plaintiff, and the proceeds were received into its treasury. It claimed that distilling spirits was beyond its powers, and therefore that the distilling was to be considered the act of its officers, and not of itself. The court crashed through this argument. The opinion was written by Mr. Justice Miller (who had dissented in National Bank *v.* Matthews on the ground that the mortgage was "void"). "But the argument is unsound that whatever is done by a corporation in excess of the corporate powers, as defined by its charter, is as though it was not done at all. . . . A municipal corporation cannot, any more than any other corporation or private person, escape the taxes due on its property, whether acquired legally or illegally, and it cannot make its want of legal authority to engage in a particular transaction or busi-

[1] See also Union Trust Co. *v.* Illinois Midland Co., 117 U. S. 434.

ness a shelter from the taxation imposed by the government on such business or transaction by whomsoever conducted" (pp. 260, 262).

Fritts v. *Palmer*, 132 U. S. 282. Corporations were forbidden to "purchase or hold real estate . . . except as provided in this act." Corporation M assumed to purchase Blackacre from A, and did not proceed according to the act. The deed was recorded. M assumed to mortgage the land, and, on foreclosure of the mortgage, B purchased. A granted to C. C was not permitted to maintain ejectment against B. The court relied on National Bank *v.* Matthews, and said (p. 293): "The question whether a corporation, having capacity to purchase and hold real estate for certain defined purposes, or in certain quantities, has taken title to real estate for purposes not authorized by law, or in excess of the quantity permitted by its charter, concerns only the state within whose limits the property is situated. It cannot be raised collaterally by private persons unless there be something in the statute expressly or by necessary implication authorizing them to do so." [1]

Case v. *Kelly*, 133 U. S. 21 (1889). A railroad company asked the court to impose a trust upon certain lands in its favor. The ownership by it of such lands was *ultra vires*. The court declined to give the relief. "The question here is, not whether the courts would deprive [the corporation] of such lands if they had been conveyed to it, but whether they will aid it to violate the law and obtain a title which it has no power to hold. We think the questions are very different ones" (p. 28).

In 1890, *Central Transportation Co.* v. *Pullman's Car Co.* 139 U. S. 24 (cited above), was decided. "*The objection to the contract is, not merely that the corporation ought not to have made it, but that it could not make it.*"

In *Logan County Bank* v. *Townsend*, 139 U. S. 67 (reported immediately after the Central Transportation Co. case), A assumed to sell to corporation M certain bonds the purchase of which was *ultra vires*. M promised to return the bonds on payment of a certain sum, and later refused to do so. In adjusting the rights of the parties, the court held that M could hold the bonds as security for the money advanced to the plaintiff, and relied upon National Bank *v.* Matthews.

In *Jacksonville Railway* v. *Hooper*, 160 U. S. 514, 524 (1895), the

[1] *Cf.* Chattanooga Ass'n *v.* Denson, 189 U. S. 408.

court, in an emphatic *dictum*, approved the reasoning of Mr. Justice Gray in the Central Transportation Co. case.

McCormick v. *Market Bank*, 165 U. S. 538 (1897). A national bank assumed to take a lease of property before it had been authorized by the Comptroller to transact business. In an opinion written by Mr. Justice Gray the court declared the lease to be "void" (p. 553). The Central Transportation Co. case is followed, and National Bank *v.* Matthews is disposed of by saying that it "depended upon section 5137 of the Revised Statutes, specifying the purposes for which a national bank might purchase, hold and convey real estate, which, as construed by the court, did not make void mortgages taken for other purposes by a banking association authorized to transact business."

In 1897 came *California Bank* v. *Kennedy* (cited above). In this case the court did not mention in any way National Bank *v.* Case, 99 U. S. 628, 633, or Salt Lake City *v.* Hollister, 118 U. S. 256. The court said that National Bank *v.* Matthews had been distinguished in McCormick *v.* Market Bank.

Sioux City Co. v. *Trust Co.*, 173 U. S. 99 (1898). The court said it would follow the interpretation of a state statute by a state court to the effect that an *ultra vires* act was not void, but only voidable.

Concord Bank v. *Hawkins*, 174 U. S. 364 (1898). California Bank *v.* Kennedy was followed.

Scott v. *Deweese*, 181 U. S. 202 (1900). No increase of the stock of M was to be "valid" until the Comptroller gave a certain certificate. M assumed to increase its stock, but the Comptroller never gave the required certificate. A assumed to purchase some of this stock, and the question was whether he could be held to the liabilities of a stockholder. The court held that he could be so held. National Bank *v.* Matthews was mentioned as a case the doctrine of which had been often reaffirmed. The increase of stock without the Comptroller's certificate was a matter between the corporation and the government under whose laws it was organized. The difference between the case at bar and the California Bank case was apparent, — A had power to take stock in M, and could therefore be estopped to say the issue was not lawful.[1]

Lantry v. *Wallace*, 182 U. S. 536 (1900). Corporation M assumed to purchase some shares of its own stock. This purchase was *ultra*

[1] *Cf.* Scovill *v.* Thayer, 105 U. S. 143.

vires. It thereafter sold the shares to A, and the court held that A might be held to the liabilities of a shareholder. "It cannot be held that the purchase by the bank of its own shares of stock was void" (p. 552).

In *O'Brien* v. *Wheelock*, 184 U. S. 450, 490 (1901), there is a *dictum*: "In the instance of contracts of a corporation beyond the scope of its corporate powers, the law is well settled in this court that nothing which has been done under them or the action of the courts can infuse any vitality into them."

Schuyler National Bank v. *Gadsden*, 191 U. S. 451, 458 (1903). The court proceeds on the principle of National Bank *v.* Matthews, and denies collateral attack.

National Bank v. *Converse*, 200 U. S. 425 (1905). The court proceeds on the principle of California Bank *v.* Kennedy, and permits collateral attack.

Blair v. *Chicago*, 201 U. S. 400, 450 (1905). The court said that the city of Chicago was not in a position to raise the question whether certain leases were not void for want of corporate power in the companies to make or receive them.

Merchants Bank v. *Wehrmann*, 202 U. S. 295 (1905). California Bank *v.* Kennedy was followed.

The people of the United States are eager to find in the decisions of the Supreme Court the most admirable results of the exercise of the judicial function. It would seem not to be a lack of real and proper respect for that court to say that its manner of handling *ultra vires* problems is most disappointing. There are two modes of thought, quite inconsistent with each other, used in its decisions. Sometimes it acts upon the one, sometimes upon the other. Upon any new question, it would be just a gamble as to which line of decisions would be followed.

The reasoning of Mr. Justice Gray in the Central Transportation Co. case is a source of great confusion. It is the revival of an antiquated conception of corporate action. It announces a sweeping rule, and yet the sweeping application of the rule would produce such monstrous results that no court would so apply it.

The court ought frankly to discard it, and to recognize that it cannot properly dispose of the *ultra vires* contracts and conveyances of a corporation as though they were the contracts and con-

veyances of a married woman or a monk under the common law.

In considering assumed corporate action by persons who have not been incorporated *de jure*, the courts carefully consider the circumstances, and determine whether or not there are sufficient reasons for denying collateral attack upon the formation of the corporation. In considering assumed corporate action by incorporated persons outside the scope of their powers, the courts should likewise carefully consider the circumstances and determine whether or not there are sufficient reasons for denying collateral attack upon the powers of the corporation. The courts have a duty, in both cases, to determine whether it is ever proper for them to give legal validity to unauthorized corporate action as corporate action.

It is submitted that the real question is, not whether there should be any doctrine denying collateral attack upon the powers of a corporation, but what should be the scope of such a doctrine.

This article deals specifically only with the question whether an executed transaction shall be a foundation of rights and liabilities.

Suppose that A assumes to convey to corporation M real or personal property which M is not authorized to take or hold, and that M thereafter assumes to convey it to B. Where is the title? If the transaction between A and M is "void," it is in A.

Granted that there was objection to M's ownership, that ownership has ceased. Let the *ultra vires* past bury its wrong. To hold the transaction to be "void" would render it highly dangerous for any one to purchase any property which any corporation had theretofore assumed to own, — and very large quantities of property have ostensibly been in corporate ownership at some time. The great public inconvenience which would result from any other rule has led the courts to deny collateral attack upon the powers of a corporation, when the only question presented is as to the power of the corporation to be a conduit of title. The authorities on this point are uniform.[1]

[1] Ayers *v.* The South Australian Banking Co., L. R. 3 P. C. 548, 549 (1871). Lord Justice Mellish said: "There may be also question whether, under any circumstances, the effect of violating such a provision is more than this, that the Crown may take advantage of it as a forfeiture of the charter, but the only point which it appears to their Lordships is necessary to be determined in the present case is this, that whatever effect such a clause may have, it does not prevent property passing, either in goods or

Suppose, now, that A assumes to convey Blackacre to corporation M, and that M is not authorized to take or hold it, and M assumes to retain the property, so that the question is whether M is entitled to the rights, and is subject to the liabilities, which are the usual incidents of ownership.

The question may present itself in a number of ways.

1. A may seek to repudiate what he has done, and to claim still to be the owner of Blackacre. He may seek to maintain ejectment, or to have the deed to M removed as a cloud on his title. No court permits him to do so.[1] It is, however, to be conceded that to deny A relief does not necessarily require a court to hold that the executed *ultra vires* transaction is a foundation of rights in the corporation.

The court may decide the case on the ground that, if the title did

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in lands under a conveyance or instrument which, under the ordinary circumstances of law, would pass it. . . . Their Lordships are of opinion that whatever other effect it has, it cannot have the effect of preventing the property passing. If that were otherwise, the consequences might be most lamentable, because if the property never passed to them, they could not themselves convey any property to third persons. . . . Mr. Manisty admitted that he could find no authority for the proposition that any violation of such a condition of a charter would prevent the property in goods passing to the person to whom an instrument otherwise valid professes to pass it." See also Durham Building Society, 12 Eq. 516; Dronfield Coal Co., L. R., 17 Ch. D. 76, 97; Batson *v.* London School Board, 20 T. L. R. 22.

Morris *v.* Hall, 41 Ala. 510, 537; Sherwood *v.* Alvis, 83 Ala. 115 (A mortgages to M, B purchases at the foreclosure sale, and may maintain ejectment against A); Bigsbee Co. *v.* Moore, 121 Ala. 379 (M subscribed to and took stock in N, and transferred to A. A may recover dividends from N) ; Barnes *v.* Suddard, 117 Ill. 237; Lathrop *v.* Commercial Bank, 8 Dana (Ky.) 114; Shewater *v.* Perrier, 55 Mo. 218; Ryan *v.* McElroy, 98 Mo. 349; Parish *v.* Wheeler, 22 N. Y. 494, 504; Matter of Long Acre Co., 188 N. Y. 361, 369; Mallett *v.* Simpson, 94 N. C. 37, 41; Leazure *v.* Hillegas, 7 S. & R. (Pa.) 313; Goundie *v.* Northampton Water Co., 7 Pa. St. 233; Gilbert *v.* Hol, 2 S. Dak. 164; Fritts *v.* Palmer, 132 U. S. 282; Lantry *v.* Wallace, 182 U. S. 536.

The grantee, B, from M, contracts to sell to C. B may have specific performance. Walsh *v.* Barton, 24 Oh. St. 28.

[1] Long *v.* Georgia Ry. Co., 91 Ala. 519, 521; Hough *v.* Cook County Land Co., 73 Ill. 23; Hayden *v.* Hayden, 241 Ill. 183; Ragan *v.* McElroy, 98 Mo. 349; Pittsburgh Co. *v.* Altoona Co., 196 Pa. 452. See also Miner's Ditch Co. *v.* Zellerbach, 37 Cal. 543, 606; Barrow *v.* Nashville Co., 9 Humphrey (Tenn.) 304.

Similarly as to any privy of A. Lathrop *v.* Commercial Bank, 8 Dana 114; Baker *v.* Northwestern Co., 36 Minn. 185; Christian Union *v.* Yount, 101 U. S. 352, 361.

Conversely the corporation cannot sue A to recover back the purchase price. Hagerstown Mfg. Co. *v.* Keedy, 91 Md. 430. To the same effect is Baird *v.* Bank of Washington, 11 S. & R. (Pa.) 411, 418.

A had land bounded by a lake. He deeded it to M, whose purchase was *ultra vires*. A has not thereafter the rights of a riparian proprietor against third parties. Attorney-General *v.* Smith, 109 Wis. 532.

not pass to M, in any event it passed out of A into the associates considered as so many natural persons.[1]

Or the court may refuse relief to A on the ground that A had been a party to an illegal transaction, and was not a proper subject for any relief. This is a doctrine stated in some opinions of the Supreme Court of the United States, notably those written by Mr. Justice Gray. He reasons thus: Everybody who deals with a corporation is charged with constructive notice of its powers. An *ultra vires* act is an illegal act. Therefore A, when he participated in the act, was *particeps criminis*.[2]

This is a ferocious doctrine. Unauthorized corporate action, simply because it is unauthorized, cannot with any propriety be said to be criminal. It is not even illegal, if that adjective is used to connote something particularly reprehensible, and not simply to connote something which is contrary to law.

In order to be incorporated, associates must file a certificate containing certain statements in a public office. A paper is filed, but it does not contain all the requisite statements. A contracts with the associates as a corporation. Here is unauthorized corporate action, and there is just as much reason for charging A with notice of the contents of the defective certificate, as there would be for charging him with notice of its contents if it had been in due form. It has never occurred to any court to call A "*particeps criminis*" under such circumstances; on the contrary, the courts are very liberal in giving A relief against the associates as a corporation.[3]

This ground for denying relief to A does not therefore commend itself.

The proper ground for denying relief would seem to be that, as a question of policy, the executed *ultra vires* transaction shall, apart from special circumstances, be a foundation of rights in the corporation. This would follow if the court took that position in the further cases to be considered.

2. A may get back the possession of Blackacre, or X, a casual trespasser, may get the possession, and M may wish to maintain ejectment. Certainly ejectment ought to lie either by M, or by the persons incorporated as so many natural persons. If ejectment is

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[1] See 20 HARV. L. REV. 470, note 23.

[2] St. Louis Railroad *v.* Terre Haute Railroad, 145 U. S. 393.

[3] See 20 HARV. L. REV. 456, and 21 HARV. L. REV. 305.

brought by M, there are no considerations of fairness in favor of A or X which require that they should be allowed collaterally to attack the power of M to be the owner of Blackacre. To determine whether the holding of Blackacre was, or was not, *ultra vires* might, and probably would, be anything but a simple matter and the determination of it would consume the time of the court. The defence of A or X, if established, would be merely technical. These are sufficient reasons for denying collateral attack by A or X.[1]

3. A tax might be assessed to M upon the land. To allow M to assert its own lack of power to escape the tax is to allow it to take advantage of its own wrong. It should not have the rights of ownership, without the liabilities.[2]

4. M may contract to convey the land to Y, and may thereafter ask for specific performance of the contract. M is now seeking, not to acquire, but to purge itself of something which it is unauthorized to have. We have already seen that the title if taken by Y will be

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[1] M may enjoin A, or a privy of A, from interference with the property. Alexander *v.* Tolleston Club of Chicago, 110 Ill. 65; Reynolds *v.* Crawfordsville Bank, 112 U. S. 413.

M may cause A to be indicted for a trespass upon Blackacre, which trespass is criminal because the ownership is in M, a municipal corporation. Commonwealth *v.* Wilder, 127 Mass. 1.

A sold a three-quarters interest in Blackacre to B, and a one-quarter interest to M. The land was sold to satisfy a lien in favor of A's grantor. The whole lien was satisfied out of B's share of the proceeds, on principles which would hold if M acquired title to the one-quarter. B was not allowed to show that M's taking was *ultra vires*. Litchfield *v.* Preston, 98 Va. 530.

A conveyed to B, the conveyance being voidable because of the fraud of B. B conveyed to M, who paid value and had no notice of the fraud. M has the rights of a *bonâ fide* purchaser against A. Schneider *v.* Sellers, 98 Tex. 380.

M may maintain ejectment against the casual possessor. Natoma Co. *v.* Clarkin, 14 Cal. 544, 552; Chicago R. R. Co. *v.* Keegan, 185 Ill. 70. *Contra*, Catholic Congregation *v.* Germain, 104 Ill. 440 (but see Hamsher *v.* Hamsher, 132 Ill. 273, 286).

If the municipality damages Blackacre by changing the grade of the street, M may recover damages. Louisville Property Co. *v.* Nashville, 114 Tenn. 213 (foreign corporation).

M may lease Blackacre to B, and maintain an action for the rent against the lessee, Rector *v.* Hartford Deposit Co., 190 Ill. 380, and the surety of the lessee, Nantasket Co. *v.* Shea, 182 Mass. 147. It may enforce other provisions of the lease. Springer *v.* Chicago Trust Co., 202 Ill. 17; Cowell *v.* Springs Co., 100 U. S. 55, 60.

M may maintain a petition under the Burnt Records Act to confirm its title. Cooney *v.* Booth Packing Co., 169 Ill. 370.

M may acquire, by accretion, more land than it is authorized to hold and may maintain a bill to quiet its title to such land. Chesapeake Co. *v.* Walker, 100 Va. 69.

[2] National Bank *v.* Case, 99 U. S. 628; Salt Lake City *v.* Hollister, 118 U. S. 256.

unimpeachable. There is therefore no sufficient reason why the courts should not hold that M has a marketable title and grant it specific performance.[1]

So much as to land. Similarly it has been held in a variety of circumstances where M has assumed, *ultra vires*, to purchase a chattel,[2] or a negotiable instrument,[3] or a non-negotiable chose in action,[4] that M might enforce the usual incidents of ownership.

May it then be laid down as a general rule that an executed *ultra vires* transaction is a foundation of rights and liabilities?

Suppose that M purchased shares of stock in another corporation, N, and that the purchase was *ultra vires* of M. A usual incident of ownership of shares of stock is the right to vote. Yet it may be improper to permit M to vote. Why? The law forbids one corporation to own shares of stock in another corporation, largely to prevent one corporation from controlling, or influencing, the management of rival corporations. To permit M to vote might be to permit the very evil intended to be prevented. It would be at the expense

[1] If B contracts to buy, M may have specific performance. See Davis *v.* Old Colony R. R., 131 Mass. 258, 273; Lancaster *v.* Amsterdam Improvement Co., 140 N. Y. 576, 584; Banks *v.* Poitiaux, 3 Randolph 136.

A municipality could compel the sale to it of the property of a water company at a valuation, and sought so to do. It was obliged to pay for all the property held by the company for the purposes of its incorporation, whether that was in excess of the amount authorized or not. West Springfield *v.* Aqueduct Co., 167 Mass. 128.

If M conveys to B, M may recover from B the purchase price. Holmes & Griggs Co. *v.* Holmes & Wessell Co., 127 N. Y. 252, 260; Fayette Land Co. *v.* Louisville R. R., 93 Va. 274 (vendor's lien in M enforced); Rutland Co. *v.* Proctor, 29 Vt. 93.

[2] Ayers *v.* The South Australian Banking Co., L. R., 3 P. C. 548 (M maintains trover against privy of A); Morris *v.* Hull, 41 Ala. 510, 537 (A may not maintain trover against M); Edwards *v.* Fairbanks, 27 La. Ann. 449 (judgment creditors of A seize the chattels, and M is allowed to intervene in the execution proceedings and recover the goods); Slater Woollen Co. *v.* Lamb, 143 Mass. 420 (M sells the chattels to B, and may recover "on the contract").

Contra, Trustees *v.* Dickenson, 1 Dev. L. (N. C.) 189 (M may not maintain detinue for slaves. Decided in 1827).

[3] If M makes an *ultra vires* purchase of a negotiable instrument, it may enforce the note against prior parties. Prescott National Bank *v.* Butler, 157 Mass. 548 (and prior cases); Merchants Bank *v.* Hansen, 33 Minn. 40 (directly overruling Farmers Bank *v.* Baldwin, 23 Minn. 198, and Bank of Rochester *v.* Pierson, 24 Minn. 140); Hennessy *v.* St. Paul, 54 Minn. 219, 223; Franklin Institution *v.* Roscoe, 75 Mo. 408.

Contra, Lazear *v.* National Union Bank, 52 Md. 48, 125 (but see United German Bank *v.* Katz, 57 Md. 128, 141; Black *v.* Bank of Westminster, 96 Md. 399, 429).

[4] If M makes an *ultra vires* purchase of a non-negotiable chose in action, it may enforce it in the same manner in which any other assignee could have enforced it. State Ins. Co. *v.* Farmers Co., 65 Neb. 31, 41; Farwell Co. *v.* Wolf, 96 Wis. 10.

of N, an innocent party. Collateral attack may properly be allowed, even in considering an executed transaction, if the denial of such attack would be to the substantial prejudice of an innocent party.[1]

It may, however, safely be said that the circumstances are special and exceptional where collateral attack should be allowed, if the corporation seeks to assert the rights of ownership usually incident to an executed transaction. Should the converse be true? Should a corporation which has the benefits of ownership be allowed to escape the liabilities? Is the result (as distinguished from the reasoning) in California Bank *v.* Kennedy sound?

It may be urged that this result is sound, since it protects the shareholders from losses attendant upon improper investments by the officers of the bank. This raises a fundamental question: for what acts, not done by the authority of the associates, is the corporation responsible? Certainly not every act done by an officer in the name of the corporation is to be considered the act of the corporation. Persons who deal with the officers of a corporation are, at least, charged with a duty to make reasonable inquiry as to whether the act is *ultra vires* of the corporation, and, if the act is *ultra vires*, and such reasonable inquiry would disclose this, no outsider can charge the corporation with any liability because of the act, unless the entire body of shareholders has ratified the act, in fact or in law.[2] It may therefore be that the corporation can defend against liability, on the

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[1] If M makes an *ultra vires* purchase of shares of stock in N, N cannot be compelled to register M as a shareholder. Franklin Bank *v.* Commercial Bank, 36 Oh. St. 350.

Even if M is registered as a shareholder it may not have the right to vote. Memphis *v.* Woods, 88 Ala. 630; Jackson *v.* Newman, 51 La. Ann. 833; Coler *v.* Tacoma Co., 65 N. J. Eq. 347; Milbank *v.* New York R. R., 64 How. Pr. (N. Y.) 20; Parsons *v.* Tacoma Co., 25 Wash. 492, 508. See also Dunbar *v.* Am. Tel. Co., 224 Ill. 9; Bigelow *v.* Calumet Co., 155 Fed. 869.

As further illustrating the principle of the text see Straus *v.* Eagle Insurance Co., 5 Oh. St. 59 (to be read with White's Bank *v.* Toledo Co., 12 Oh. St. 601, 610). A insured with M, and suffered a loss. M made an *ultra vires* purchase of a note by A. M was not allowed to set off the note against A's claim.

See also Central R. R. Co. *v.* Penn. R. R. Co., 31 N. J. Eq. 475, 495.

[2] This is a topic the adequate discussion of which would in itself take an article. See *In re* European Society Arbitration Acts, L. R. 8 Ch. D. 679; Central Co. *v.* Smith, 76 Ala. 572.

In California Bank *v.* Kennedy, one ground of defense was that the stock was issued to it without due authority from it in its corporate capacity. But this point was not discussed.

ground, not that it could not purchase, but that it did not, — that the purchase was not an act for which it is responsible.

Suppose, however, that the entire body of shareholders does ratify the act. The Supreme Court doctrine is that this makes no difference. "The transaction being absolutely void, could not be confirmed or ratified." This is a doctrine that the shareholders of a corporation, M, can authorize or ratify the purchase of shares in another corporation, N, that M can receive dividends upon the shares so long as N flourishes, but can then take advantage of its own wrong and repudiate all liability when N becomes embarrassed, and its innocent creditors seek to hold its shareholders to their liability. To such a result does the reasoning of Mr. Justice Gray lead. It seems flatly wrong, and to deserve the strictures which have been made upon it in some of the state courts.[1]

This article has dealt only with absolute transfers *inter vivos*. There seems to be, on principle and authority, no doubt but that such transactions may properly be regarded as executed. Whether mortgages, leases, devises, and bequests are to be regarded as executed or executory transactions are questions postponed to a subsequent article.

In conclusion it is submitted: (1) that the reasoning of Mr. Justice Gray in Central Transportation Co. *v.* Pullman's Car Co. is fallacious and mischievous, strongly resembling the reasoning in the very early authorities to the effect that a corporation *could* not commit a tort, and that this reasoning cannot be made the basis of any harmonious and equitable system of law to govern *ultra vires* transactions; (2) that a doctrine that collateral attack upon the powers of a corporation may be denied is unobjectionable in theory, and beneficial in application, and the courts have a duty to determine the proper scope of such a doctrine; (3) that if the *ultra vires* transaction is executed, and the sole question is whether the corporation was a conduit of title, collateral attack should be denied; (4) that if the *ultra vires* transac-

[1] Fidelity Insurance Co. *v.* German Savings Bank, 127 Iowa 591; Hunt *v.* Hansen Malting Co., 90 Minn. 282; Security Bank *v.* St. Croix Co., 117 Wis. 211, 218. See also Turtelot *v.* Whithed, 9 N. Dak. 467, 476; Wright *v.* Pipe Line Co., 101 Pa. St. 204.

The doctrine of the United States Supreme Court was followed in Chemical Bank *v.* Havermale, 120 Cal. 601; Leonhardt *v.* Small, 117 Tenn. 153; Converse *v.* Emerson Co., 90 N. E. 269 (Ill.).

tion is executed, and the corporation seeks to assert the rights usually incident to ownership, collateral attack should, as a general but not universal rule, be denied; (5) that if the *ultra vires* transaction is executed, and the corporation seeks to repudiate the liabilities usually incident to ownership, collateral attack should be denied.

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